

**STATE OF WASHINGTON
OFFICE OF THE INSURANCE
COMMISSIONER**



FINANCIAL EXAMINATION
of the Charitable Gift Annuity Business
of

**Virginia Mason Health System
Seattle, Washington**

DECEMBER 31, 2004

Order No. G 07-29
Virginia Mason Health System
Exhibit A

SALUTATION

Seattle, Washington
April 4, 2007

The Honorable Mike Kreidler, Commissioner
Washington State Office of Insurance Commissioner (OIC)
Insurance Building–Capital Campus
302–14th Avenue SW
Olympia, WA 98504

Dear Commissioner Kreidler:

In accordance with your instructions and in compliance with the statutory requirements of Chapter 48.38 RCW, Charitable Gift Annuity (CGA) business, an examination was made of the corporate affairs and financial records of the CGA business of

Virginia Mason Health System

of

Seattle, Washington

hereinafter referred to as “VMHS” at its office, 1100 Ninth Avenue, Seattle, WA 98111.

This report of examination is respectfully submitted showing the condition of the CGAB of VMHS as of December 31, 2004.

CHIEF EXAMINER'S AFFIDAVIT

I hereby certify I have read the attached Report of the Financial Examination of the Charitable Gift Annuity business of Virginia Mason Health System of Seattle, Washington. This report shows the financial condition of the Charitable Gift Annuity business and related corporate matters of Virginia Mason Health System as of December 31, 2004.

A handwritten signature in black ink, reading "Patrick H. McNaughton". The signature is written in a cursive style with a horizontal line underneath.

Patrick H. McNaughton
Chief Examiner

4-4-2007

Date

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SCOPE OF THE EXAMINATION

This examination covers the period January 1, 2000 through December 31, 2004. Although the scope of our examination focused only on the transactions and operations of the CGA business, we also reviewed the financial statements of VMHS and Virginia Mason Medical Center (VMMC), a subsidiary of VMHS, to evaluate the overall financial statement presentation. VMHS' records, along with various aspects of its operating procedures and financial reports, were reviewed and tested during the course of this examination as necessary to substantiate CGA business reporting. The results of the examination are commented upon in the various sections of this report. In addition, VMHS' certified public accountant's (CPA's) reports were reviewed and utilized, where possible, to facilitate efficiency in the examination.

The examination was conducted in accordance with the statutory requirements contained in the Revised Code of Washington (RCW) and the guidelines recommended by the National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook (FCEH). The examination was conducted at the Seattle office of VMHS by examiners from the state of Washington.

INSTRUCTIONS

The examiners reviewed VMHS's CGA business annual reports as part of the statutory examination. This review was performed to determine if VMHS completed the annual reports in accordance with the Annual Report Instructions published by the OIC and to verify that VMHS's accounts and records were prepared and maintained in accordance with Chapter 48.38 RCW.

The following summarizes the exceptions noted while performing this review.

1. Reporting Requirements

VMHS reports the CGA business consolidated under an affiliate, Virginia Mason Medical Center (VMMC). VMMC's financial statements are reported separately and independently from VMHS. To correctly file the Annual Report in compliance with Chapter 48.38 RCW, the CGA business should be filed with the Certificate of Exemption holder, VMHS.

VMHS is instructed to file all Annual Reports under the legal entity granted the Certificate of Exemption in compliance with RCW 48.38.010.

COMMENTS AND RECOMMENDATIONS

None

ORGANIZATION PROFILE

History: VMHS (formerly named as VMMC prior to June 1, 1994) is a nonprofit organization established in 1986 and incorporated in the state of Washington on October 17, 1985. VMHS is the parent and sole owner of the Virginia Mason Medical Center and Benaroya Research Institute (BRI); both are Washington nonprofit corporations. VMHS raises philanthropic support through a division, Virginia Mason Foundation, to provide new facilities, equipment and comprehensive services and programs for VMMC and BRI.

Territory and Plan of Operation: On February 23, 1993, the OIC granted VMHS a Certificate of Exemption #45 to conduct a CGA business in the state of Washington. There were nineteen in-force annuity contracts as of December 31, 2004. All of the 19 annuity contracts were issued to residents of the state of Washington.

Total Net Assets: VMMC's total net assets as of December 31, 2004 were \$164,865,000. This amount included unrestricted net assets of \$156,268,000. The minimum unrestricted net asset requirement pursuant to RCW 48.38.010(6) was satisfied as of December 31, 2004. The assets met the statutory requirements, although they were incorrectly consolidated with VMMC's financial statements. (See Instruction No. 1)

Growth: The development of VMHS prior to 2003 and VMMC for the years 2003 and 2004 are reflected in the following schedules. All information was compiled from VMHS' and VMMC's audited financial statements where the CGA business transactions and account balances were accounted and reported, as of calendar years ending December 31. (See Instruction No. 1)

Schedule 1 – Statement of Financial Position

(In thousands)

<u>*Year</u>	<u>Assets</u>	<u>Liabilities</u>	<u>Total Net Assets</u>	<u>Total Net Assets Allocated Into:</u>		
				<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>
2004	\$446,563	\$281,698	\$164,865	\$156,268	\$5,514	\$3,083
2003	421,747	267,069	154,678	144,636	7,148	2,894
2002	21,467	3,014	18,453	5,907	4,994	7,552
2001	26,902	2,531	24,371	9,324	7,555	7,492
2000	33,382	2,215	31,167	9,181	14,348	7,638

Schedule 2 – Statement of Activities and Changes in Net Assets

(In thousands)

	<u>*2004</u>	<u>*2003</u>	<u>*2002</u>	<u>*2001</u>	<u>*2000</u>
Total revenues	\$606,396	\$582,330	\$3,408	\$5,136	\$11,676
Total expenses	596,640	546,693	9,326	11,932	14,980
Increase (decrease) in net assets	9,756	35,637	(5,918)	(6,796)	(3,304)
Net assets at beginning of year	154,678	119,041	24,371	31,167	34,471
Net assets at end of year	\$164,865	\$154,678	\$18,453	\$24,371	\$31,167

Number of gift annuity contracts at end of year

19 19 20 20 23

* In 2003 and 2004, the CGA business was incorrectly reported on a consolidated basis with VMMC. This is shown as a material increase in financial statement balances from 2002 to 2003. (See Instruction No. 1)

AFFILIATED ORGANIZATIONS

VMMC and BRI are subsidiaries of VMHS; all are nonprofit corporations. The financial statements of VMHS do not consolidate the financial statements of VMMC and BRI.

MANAGEMENT AND CONTROL

Management: Responsibility for the management of VMHS is vested in its Board of Directors (BOD). The number, qualifications, terms of office, manner of elections, time and place of meetings, and powers and duties of directors are prescribed by VMHS' Bylaws. VMHS is the sole corporate owner of VMMC, has overlapping members on the BOD, and reserves certain rights and responsibilities regarding governance, strategic plans and transactions.

Board of Directors: The directors as of December 31, 2004:

Carolyn Corvi	Tom O'Keefe
Michael Glenn	J. Michael Rona
Pamela Green	Pat Scott
Gary S. Kaplan	Evelyn Sroufe
Terry Macaluso	Charleen Tachibana
Robert Mecklenburg	Thomas Van Dawark
Lee Minto	David Williams
David Moffett	Jim D. Young

Officers: In accordance with the Bylaws, the executive officers of VMHS include a chair/chief executive officer (CEO), a president and other executive officers as may be deemed appropriate by the BOD, CEO or president from time to time. The executive officers are responsible for administering the operations of VMHS, including providing for compliance with applicable laws and regulations. The executive officers include:

Gary Kaplan, MD, Chairman and CEO
J. Michael Rona, President
Craig Goodrich, Sr. Vice President and Chief Financial Officer
Lynne Chafetz, Sr. Vice President and General Counsel
Michael VanDerhoef, Vice President

Tax Status: VMHS is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code.

Conflict of Interest: VMHS has a conflict of interest policy which is a part of, and is defined in its Bylaws. No exceptions were noted.

CORPORATE RECORDS

The BOD meets to discuss business which is pertinent to VMHS. Minutes of the meetings of the directors approve and support VMHS' transactions and events. No exceptions were noted.

STATEMENT OF ACTUARIAL OPINION

A consulting actuary with Milliman, Inc., reviewed the adequacy of the annuity reserves and issued a Statement of Actuarial Opinion (SAO) which stated that he is a member of the American Academy of Actuaries and meets its qualification standards. The SAO states that the annuity contract reserves computed under RCW 48.38.020(3)(a) and (b) of the Washington Insurance Code were \$551,159. This amount, plus the 10% surplus required by RCW 48.38.020(3)(c), was properly reported in VMMC's financial statements.

ANNUITY ASSETS CUSTODIAL FUNCTION

The separate reserve fund assets were held legally and physically segregated from the other assets of VMHS or VMMC. Total annuity investments as of December 31, 2004 were \$610,883 and consisted of corporate bonds.

SUBSEQUENT EVENTS

There were no material events which impacted VMHS' CGA business between the examination date and the last day of our field work.

ACCOUNTING RECORDS AND PROCEDURES

The records and source documentation supported the data and amounts presented in the annual report for the year ended December 31, 2004.

FINANCIAL STATEMENTS

The following financial information summarizes the financial statements of VMMC as of December 31, 2004. (See Instruction No.1)

Balance Sheet

	<u>Balance Per</u> <u>Annual</u> <u>Report</u>	<u>Adj.</u>	<u>Examination</u> <u>Adjustments</u>	<u>Adjusted</u> <u>Balance</u>
<u>ASSETS</u>				
Current assets	\$130,479,000			\$130,479,000
Assets whose use is limited	132,498,117			132,498,117
CGA assets	610,883			610,883
Land, buildings and equipment, net of accumulated depreciation	179,540,000			179,540,000
Deferred financing costs	2,255,000			2,255,000
Other assets	1,180,000			1,180,000
Total Assets	<u>\$446,563,000</u>		<u>\$0</u>	<u>\$446,563,000</u>
<u>LIABILITIES</u>				
Current liabilities	\$95,771,000			\$95,771,000
CGA reserves	606,275			606,275
Other liabilities	64,060,725			64,060,725
Long-term debt	121,260,000			121,260,000
Total Liabilities	<u>281,698,000</u>		<u>0</u>	<u>281,698,000</u>
<u>NET ASSETS</u>				
Unrestricted	156,268,000			156,268,000
Temporarily restricted	5,514,000			5,514,000
Permanently restricted	3,083,000			3,083,000
Total Net Assets	<u>164,865,000</u>		<u>0</u>	<u>164,865,000</u>
Total Liabilities and Net Assets	<u>\$446,563,000</u>		<u>\$0</u>	<u>\$446,563,000</u>

Statement of Financial Activity and Changes in Net Assets

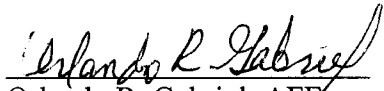
	<u>Balance Per</u> <u>Annual</u> <u>Report</u>	<u>Adj.</u>	<u>Examination</u> <u>Adjustments</u>	<u>Adjusted</u> <u>Balance</u>
Total revenues	\$606,396,000		\$0	\$606,396,000
Total expenses	(596,640,000)		0	(596,640,000)
Excess of revenue over expenses	9,756,000		0	9,756,000
Changes in net assets:				
Unrestricted	1,876,000			1,876,000
Temporarily restricted	(1,634,000)			(1,634,000)
Permanently restricted	189,000			189,000
Net assets at beginning of year	154,678,000			154,678,000
Net assets at end of year	<u>\$164,865,000</u>		<u>\$0</u>	<u>\$164,865,000</u>

ACKNOWLEDGMENT

Acknowledgment is hereby made of the cooperation extended to the examiners by the officers and employees of VMHS during the course of this examination.

In addition to the undersigned, Michael V. Jordan, CPA, CFE, MHP, Assistant Chief Examiner; and John Gaynard, CPA, CFE, FLMI, Life and Disability Field Supervising Examiner, from the Washington State Office of the Insurance Commissioner, participated in the examination and the preparation of this report.

Respectfully submitted,

A handwritten signature in cursive script, reading "Orlando R. Gabriel", written over a horizontal line.

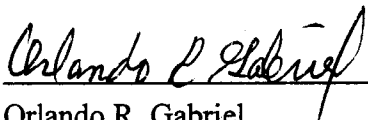
Orlando R. Gabriel, AFE
Examiner-in-Charge
State of Washington

AFFIDAVIT

STATE OF WASHINGTON }
 } ss
COUNTY OF KING }

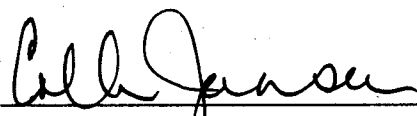
Orlando R. Gabriel, being duly sworn, deposes and says that the foregoing report subscribed by him is true to the best of his knowledge and belief.

He attests that the examination of VMHS' CGA business was performed in a manner consistent with the standards and procedures required or prescribed by the Washington State Office of the Insurance Commissioner and the National Association of Insurance Commissioners (NAIC).



Orlando R. Gabriel
Examiner-in-Charge
State of Washington

Subscribed and sworn to before me on this 4th day of April, 2007.



Notary Public in and for the
State of Washington,
Residing at Seattle.

